FILE COPY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. ~~1054~~ 48

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

vs.

JOHN STUART,

Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

GEORGE I. HAIGHT,
WILLIAM D. MCKENZIE,
HERBERT POPE,
Counsel for Respondent.

April 7, 1942.

THE BURTHORP-WARREN PRINTING COMPANY, 211 WEST JACKSON, CHICAGO

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The Petitioner in this case contends that the decision below is in conflict with decisions in other cases in other Circuit Courts of Appeal. The truth is that Petitioner's contention in this case carries the "family solidarity" argument to such an extreme that it defeats itself. There is no other case which demonstrates so conclusively that even in tax cases the line must be drawn somewhere short of complete absurdity.

In order to revest the grantor with the required ownership or control of the trust property, Petitioner is compelled, regardless of the law of Illinois, to give a construction to paragraph "Ninth" of each trust that will make the two trustees therein mentioned the individual owners of the property free from any fiduciary obligation. Then,

according to Petitioner's argument, they may, at the request of the grantor, give the trust property back to him. It is contended by Petitioner here, as it was in the Court below, that these two trustees, the wife and the brother, while not named as beneficiaries, have the power to make themselves, or to make the grantor, beneficiaries of the trust, and thus to turn the trust property back to the grantor or take it for themselves or give it to anyone else as they may see fit. Petitioner then concludes that, in view of this unlimited power in the two trustees and "in the light of the business and family relationships," (Petitioner's brief, p. 9), the complete ownership of the wife and brother becomes the ownership of the grantor, and yet asserts that the ownership of the wife and brother is not an adverse interest.

What becomes of the gift tax under this theory Petitioner does not say. Certainly a man could not make a taxable gift to his wife or his brother or to anyone else in his family group if such a theory were to prevail. At least there could be no gift until the man and his wife or his brother fell out, and only a person who was a sworn enemy of the family group could become a real trustee.

Seriously, does the Petitioner contend that the two trustees could take this trust property for their own and then after that give it back to the grantor without a gift tax? Or could they give it, as the Board Member suggested, to one of the counsel in the case without committing any breach of trust? The courts in Illinois, if proper appeal were made to them, would have the right to say something about that.

It is certain that a chancery court in Illinois would protect the named beneficiaries in these trusts if the two trustees undertook to appropriate the trust property for the benefit of themselves or the grantor or others. The highest court in Illinois would not construe paragraph

"Ninth" of these trusts as giving to the trustees an unlimited power to change beneficiaries, and it would not recognize any changes which were not the result of the exercise of the independent judgment of the two trustees. We submit that the Circuit Court of Appeals was right in its conclusion regarding the application of the law of Illinois in this case, and that the development of the federal common law in this country will not be impeded nor the "creative art" displayed in the *Clifford* case, 309 U. S. 331, impaired, if the petition for certiorari in this case be denied.

It is clear that paragraph "Eighth" of each trust, which provides that the grantor shall have the right to withdraw securities from the trust only if he replaces them with other securities of equal market value, prevents a modification of the trust under paragraph "Ninth" which would return the trust property to the grantor without the substitution of such other securities. Such a modification of the trust by the two trustees would clearly constitute a breach of trust. And it does not seem possible that such a breach of trust could be avoided if the two trustees first took the property for themselves, terminating the trust, and then returned the trust securities to the grantor. Certainly if that could be done the two trustees would in any event subject themselves to a gift tax larger than the income tax now involved. By returning the trust securities to the grantor they must be either fiduciaries committing a breach of trust or owners subjecting themselves to a gift tax; and in either case Section 166 of the Revenue Act would not apply.

It is just as clear that if the trusts are to continue they must be continued in accordance with their express terms. They are not short term trusts. They are intended for the benefit of the grantor's children, but contain provisions which direct how the property shall be held in the

event of the death of the named beneficiaries and when and to whom the trust property shall finally be distributed. There are no provisions for termination at the discretion of the trustees, and the trustees are required to act for the benefit of the beneficiaries. The grantor himself is excluded as a beneficiary and as an owner by the terms of paragraph "Eighth," and the named beneficiaries, and all other persons who conceivably might become beneficiaries, including, according to Petitioner, the two trustees, have interests adverse to the grantor. The beneficiaries are entitled at all times to insist that the trustees perform their duties as trustees. The two trustees mentioned in paragraph "Ninth" have no power to delegate any of their powers or duties to the grantor, and the named beneficiaries are entitled to appeal to a court of chancery to prevent arbitrary action by the two trustees under the powers conferred upon them by paragraph "Ninth," and to prevent any action which is not consistent with the purpose of the trusts and the intention of the grantor as shown by the trusts themselves and the testimony of the grantor.

In the Court below it was contended that the beneficiaries probably would not appeal to a court of chancery even if the trust property were returned to the grantor. But the existence of an adverse interest is not to be determined by speculation as to what the person having such an interest might do to protect it. The beneficiaries do in fact have enforceable interests adverse to the grantor, and the attempt of Petitioner to escape from that conclusion results only in giving adverse interests to the two trustees by making them in effect the owners of the trust property. As stated at the beginning, this contention of Petitioner defeats itself because it creates merely another adverse interest—an interest in the wife and brother—which eliminates the application of Section 166 and

leaves no room for argument under Section 167 or Section 22 (a) of the Revenue Act.

In none of the cases cited by Petitioner is the decision based upon the assumption of a breach of trust by trustees or the unwillingness of beneficiaries to protect their interests. It is not necessary, therefore, to refer in detail to the cases cited in order to show that the decision of the Court of Appeals in this case is not in conflict with any other decision anywhere.

Respectfully submitted,

GEORGE I. HAIGHT,
WILLIAM D. MCKENZIE,
HERBERT POPE,
Counsel for Respondent.

April 7, 1942.